

Chapter 1

An introduction to civil law

Introduction

Our lives are inextricably linked to civil law. The transactions people are a part of in life may give rise to the formation of contracts, changes in property ownership or the assumption of liabilities. People involved in estate planning may have to deal with complex issues in connection with marriage and inheritance. All these matters fall within the sphere of civil law.

But what is civil law? *The Collins Dictionary of Law* (Stewart and Burgess 1996, 68) lists a number of definitions. These include 'the domestic law of any particular nation,' 'the law of ancient Rome,' 'law or legal systems based on Roman law,' 'law that is not criminal law' and 'law that is not military law.'

In this book, 'civil law' generally refers to one branch of law or a law code in a civil law system. It is composed of principles, rules and regulations that govern property relations and personal relations, with respect to the rights and duties of persons who carry out activities of their own accord on an equal footing, subject to no interference by any state power.

The civil law system and the common law system are the two best-known legal systems in the world. The term 'civil law' as one branch of law or a law code is widely employed in civil law systems. Laws in a civil law system are principally derived from various law codes in the form of statutes (legislation). By comparison, laws in a common law system come from binding judicial precedents (case law), alongside statutes. Conventionally, a common law system does not attach great importance to a systematic demarcation of branches of law. Thus a codified civil law may not be found in a common law system. However, the main substance of civil law does exist in a common law

system. Other than being contained in a civil code, it can be found in different areas of law covering specific subject matter.

On the whole, Chinese law can be viewed as having virtually the same characteristics as those of a civil law system, in terms of the essential forms of law and general categorization of law.

The origins of civil law systems can be traced back to Roman law, which served as a basis for the subsequent development of civil law systems in other places around the globe. In light of Roman law, all law can be divided into two categories: public law and private law. Examples of public law can be cited from constitutional law, criminal law and administrative law; and examples of private law can be found in the fields of civil law and business or commercial law. In essence, civil law provides building blocks for private law, which most closely impacts business transactions and social dealings in everyday life. In this sense, civil law can be seen as the foundation of business law.

In Article 2 of China's General Principles of Civil Law (a representative Chinese statute on civil law), 'civil law' is described as the law governing property relations and personal relations forged between civil subjects (i.e. persons) of equal status, including such relations between citizens (i.e. natural persons), between legal persons, or between citizens and legal persons.

While civil law systems in different areas of the world may differ to a certain degree due to evolution and adaptation, the fundamental doctrines and structure of civil law are largely universal in civil law systems. On the whole, the contemporary civil law framework is supported by essential components, such as the General Principles of Civil Law, the law of property (the Chinese terminology is 'property rights law'), the law of contract, the law of tort (also known as 'tort liability law'), family law, the law of succession, as well as some important concepts in connection with obligations (e.g. *negotiorum gestio* and unjust enrichment).

However, as this book is business-oriented, it will not cover some civil law topics such as family law and the law of succession.

This first chapter discusses law and legal systems in a general sense before turning to the more specialized area of civil law.

Law and legal systems

This section introduces some basic information about law and legal systems, in particular the Chinese legal system.

The characteristics of law

What is law? This is not an easy question to answer. In fact, there is no standard description of law, because the meaning and spirit of law is understood from different perspectives and for different purposes by different people at different times.

For instance, according to natural law theorists, law is 'a set of moral norms' and is associated with 'justice and right, accessible to reason, which can be used as standards to judge the exercise of human power' (Waldron 2005, 181), while law is positioned in Marxist theory as 'an instrument of class domination used by a ruling class to maintain and advance its interests' (McCoubrey and White 1993, 109).

In Osborn's *Concise Law Dictionary* (Woodley 2005, 238), an entry for 'law' reads as follows:

A law is an obligatory rule of conduct. The commands of him or them that have coercive power (Hobbes). A law is a rule of conduct imposed and enforced by the Sovereign (Austin). But the law is the body of principles recognized and applied by the State in the administration of justice (Salmond). Blackstone, however, maintained that a rule of law made on a pre-existing custom exists as positive law apart from the legislator or judge.

As this book concerns Chinese law, it is essential to begin by considering how law is perceived in prevailing Chinese jurisprudence, which closely follows Marxist theory.

According to the prevailing view in Chinese academia,¹ law is created by the state at a certain point in human history; it is enforceable by state machines

¹ See, e.g. B Y Li 2001, 31–35, 49–53 and 91–94; Shen 2001, 27–31 and 38–39; and M H Wang 2005, 23–30, 35, 206–10 and 241–43.

such as judicial organs, and the police and military forces; it represents a set of norms governing human conduct (not human thought); but it governs important human conduct only, and not trifles. The following discussion is based on this view.

Law: Governing human conduct with state compulsion

Law is created by the state at a certain point in human history. It cannot be in place until certain conditions are fulfilled. Those conditions include: sovereign states coming into being, adjudication systems being available, and a sense of rights and duties becoming rooted in the human mind. Law is developed for the purpose of constructing an effective regime under which society can be kept in good order. It is enforced by the state using state machines such as judicial organs, and the police and military forces.

The evolution of law is an outcome of the complex interaction of economic, political, cultural and philosophical factors. A legal system's soundness relies on how economic fruition is achieved at various levels in society, and its success depends on whether the state is able to render abiding protection and respect for the rights and duties of its citizens (especially relating to the protection of the assets of private individuals).

In essence, the law charts a course for human conduct. The cardinal rights and duties of human beings are encapsulated in the law, which in turn provides a mechanism for safeguarding those rights and duties.

By formulating a series of bottom-line norms, law governs human conduct. But law does not govern human thought. In other words, people can be punished by law for what they have done, but not for what they have thought. So, if Jack hates Jill and kills her, Jack will be charged with murder. However, if Jack hates Jill but does not take action, Jack will not face a charge.

Law, moral teaching and religious doctrine can all be categorized as norms employed to guide human conduct. Although the law may embrace elements of morality and religion to various degrees, moral teaching or religious doctrine are no substitute for law and have no binding force in a court of law. Only law can be enforced by relying on state compulsion through state machines like judicial organs, and the police and military forces. In other

words, only law can generate a compulsive force for governing human behaviour. For example, although Catholic churches are strongly against abortion, a Catholic woman who chooses to have an abortion does not break the law.

The legitimacy and authority of law comes from its rationality. Rationality can be acquired from classroom theory or practical experience. The rationality of law is to a large extent derived from practical experience. Law reveals the collective rationality of humankind. In a democratic society, such collective rationality is usually a result of a democratic process (e.g. the establishment of a legislature through universal suffrage). Without the rationality of law, legal civilization and justice could not be achieved in the modern world (and people might, for example, still face Medieval-style 'trial by ordeal,' which used torture, such as trial by water, to judge guilt or innocence in the name of God's will).

Law: Governing important human conduct only

A legal proverb says 'the law does not concern itself with trivial matters' (*de minimis non curat lex*). This is true in today's complex society: given the limited legislative and judicial resources available to the state, law can only focus on tackling matters that are of great significance to the well-being of the people and society.

For the parties involved, taking court action is both expensive and time-consuming, and, worse still, casts a shadow over human relations. Averting unnecessary legal action is held in particularly high regard by the Chinese, who are inclined towards maintaining good relations with other people and find this a key to achieving success in business transactions and social dealings. There are some far less drastic ways of settling disagreements or disputes than bringing a case to court, e.g. conciliation, negotiation and arbitration.

The goals of law

The goals of law can be viewed as justice, rights and order. These contribute to the ultimate goals of peace, freedom and happiness.

Constitutional Law (revised in 2004) made it clear that legitimate private assets are 'inviolable.' The enactment of the Property Rights Law in 2007 reinforced this mandate, and can be viewed as a milestone of pragmatism in the development of China's legal framework within which both public and private assets are envisaged to be safeguarded equally.

This chapter discusses the main features of property rights and analyses how the Property Rights Law is structured, why it is needed in China and how the three cardinal principles advocated under the law should be understood and applied. It then focuses on several key areas of the law: the formation and alteration of property rights; ownership; usufructuary rights; and property rights relating to security.

The promulgation of the Property Rights Law

This section examines how the Property Rights Law was promulgated in China. The first question that needs to be addressed is: what exactly are property rights?

The definition of 'property rights'

The term 'property' under the Property Rights Law covers 'immovable property' and 'movable property' (Article 2, paragraph 2).

By Article 2, paragraph 3, a 'property right' is viewed as the right over specific property entitling the right holder to directly and exclusively control the property in question; such right may refer to ownership, usufructuary rights or property rights relating to security.

The exclusive nature of a property right lies in the right holder's eligibility to monopolize the property to such an extent that his property right is enforceable against anyone in the world (other than himself).

For example, the statement 'I have a luxury watch worth RMB 500,000' displays my ownership of this watch: I am entitled to exercise my exclusive property right over the watch entirely at my discretion. I can decide whether

I want to wear it myself or give it to a friend as a gift. No one is allowed to interfere in how I use the watch or the way I dispose of it (if I am willing to do so).

Sun (2008, 9) gives a good description of the features of a property right using the idea of 'three specifics': 'a specific right over a specific property held by a specific person.'

As noted in Chapter 2, laws on things under the conventional civil law regime include the law of property (i.e. the Property Rights Law) and the law of obligations. As opposed to the term 'property right' used under the law of property, the right is called the 'obligee's right' (more commonly known as the 'creditor's right') in the law of obligations.

The obligee's right is closely connected with the obligations that arise from the established property relations as identified in the General Principles of Civil Law (GPCL), Chapter 5, Section 2. In light of Article 84, paragraph 1 of the GPCL, obligations are understood as emanating from a relationship created between two parties, with the party who is entitled to enjoy rights as the obligee (the creditor) and his counterparty who has to fulfil obligations as the obligor (the debtor). According to Article 84, paragraph 2 of the GPCL, the obligee has the right to request the obligor to fulfil the latter's obligations in line with a contract or pursuant to the law.

However, unlike a property right, which is of an exclusive nature and can be defended against claims made by anyone (other than the right holder) over such right, the obligee's right can only be enforced against the obligor (i.e. his debtor) and not against anyone else. For example, the statement 'T owes G RMB 500,000' illustrates the obligee's right held by G over T: only G as the obligee (the creditor) is entitled to seek repayment of that RMB 500,000 from T; and, by the same token, only T as the obligor (the debtor) has to fulfil his obligation of repaying G.

This illustrates the main difference between a property right under the law of property (i.e. under the Property Rights Law) and the obligee's right under the law of obligations.

The structure of the Property Rights Law

In March 2007, the National People's Congress passed the Property Rights Law, which became effective in China on 1 October 2007.¹

The Property Rights Law comprises five parts. General provisions are contained in Part 1, and specific provisions in Parts 2 to 5.

Part 1, 'General provisions,' includes the following topics: cardinal principles; the creation, modification, transfer and termination of property rights (registration of immovable property, delivery of movable property, and other rules); and the protection of property rights. The rules derived from the general provisions contained in Part 1 apply to the specific provisions included in Parts 2 to 5.

The title of Part 2 is 'Ownership,' and it includes the following topics: general rules; state ownership, collective ownership and private ownership; ownership in a condominium; a neighbouring relationship; co-ownership; and special rules on acquiring ownership.

The title of Part 3 is 'Usufructuary rights,' and it includes the following topics: general rules; the right to use contracted farmland; the right to use land for construction purposes; the rural household's right to use land for residential purposes; and easement.

The title of Part 4 is 'Property rights relating to security,' and it includes the following topics: general rules; mortgages (ordinary mortgages and maximum mortgages); pledges (pledges of movable property and pledges of right); and liens.

The title of Part 5 is 'Possession,' which refers to the situation in which a property (either immovable or movable) is physically kept by a person who temporarily or permanently controls it.

1 A Chinese version of the Property Rights Law can be found at: http://www.gov.cn/jifg/2007-03/19/content_554452.htm. There is no official English version of the Property Rights Law at present. English translations can be found in various sources, where the translations differ. The author uses his own English translation in this book.

The English translation at the following website can also be used as a reference: http://www.lehmanlaw.com/fileadmin/lehmanlaw_com/laws_regulations/Propoerty_Rights_Law_of_the_PRC_LLX_03162007.pdf.

Under Article 2, paragraph 1, the Property Rights Law positions itself as a set of legal regulations governing the 'attribution and utilization of property.' The attribution of property, which is established by the ownership of property, is the core, based on which the utilization of property relies on some other kinds of property rights like usufructuary rights and property rights relating to security (in connection with mortgages, pledges or liens).

While ownership, usufructuary rights and property rights relating to security all fall within the scope of property rights, possession (as the main theme in Part 5 of the Property Rights Law) is not a property right, but refers to a situation in which a property is physically occupied by a person, which is a status that protects against any unauthorized or illegitimate occupancy of that property.²

The passage of the Property Rights Law

There was fierce debate in China about whether the Property Rights Law was needed. It took over 13 years from the first draft to final ratification for the law to be passed, longer than for any other law in China, and drafts were deliberated at the Standing Committee of the National People's Congress and the National People's Congress eight times in total (Wei 2008, 491–92).

The official view in China on the promulgation of the law can be identified in the following extract from the speech 'Explanation on China's Draft Property Rights Law' delivered by Wang Zhaoguo, vice-chairman of the Standing Committee of the National People's Congress, at the Fifth Session of the Tenth National People's Congress in 2007 (Xinhua 2007b):

The property law is a basic civil law that serves to regulate property relationships and adjust civil relationships stemming from attribution and the use of things, and it involves defining the property of the State, the collective, individual and other obligees and protecting property.

2 By Article 245 of the Property Rights Law, where the legitimately possessed property (either immovable or movable property) is illegally seized or impaired, the possessor will be entitled to claim for the return of the property within one year after the seizure, or for the elimination of the impairment; and will be eligible to seek compensation for any loss incurred due to such seizure or impairment.

China's General Principles of the Civil Law, Land Administration Law, Law on the Administration of the Urban Real Estate, Law on Land Contract in Rural Areas, Guarantee Law, etc., include not a few provisions on property, which have played an important role in economic and social development. As the reform deepens, the opening-up extends and the socialist economy, politics, culture and society moves forward, in order to meet the requirements of materializing in an all-round way the scientific concept of development and building of a socialist harmonious society, it is necessary to enact a property law, in accordance with the Constitution and on the basis of experience gained through practice, to stipulate for questions of a general character in the property system and questions in real life calling for urgent regulation, thus further defining the attribution of things to avoid disputes, bring into full play the usefulness of things, protect the property of the obligees and improve the Chinese-style socialist property system.

Enacting the property law is necessitated by the need to uphold the basic socialist economic system. Keeping public ownership dominant and having the economic sectors of diverse forms of ownership develop side-by-side constitute the basic socialist economic system of the State in the primary stage of socialism. Enactment of the property law will serve to define the scope of State-owned property and collective-owned property and the exercise of State ownership and collective ownership and strengthen protection of State-owned and collective-owned property, and will be conducive to consolidating and developing the economic sector of public ownership; and it will serve to define the scope of private property and protect private property in accordance with law, which will be conducive to encouraging, supporting and guiding the development of the economic sector of non-public ownership.

Enacting the property law is necessitated by the need to regulate the order of the socialist market economy. Clear-cut definition of property and fair competition are the basic requirements for developing the socialist market economy. Enactment of the property law will serve to confirm the attribution of things, specify the contents of ownership. Usufruct and security rights, ensure the equal legal status of the various market subjects and their right to development and protect the property of the obligees in accordance with law — all this will play an important role in developing the socialist market economy.

Enacting the property law is necessitated by the need to safeguard the immediate interests of the people. As the reform and opening-up and the economy develop, people's living standards have improved in general, and they urgently require effective protection of their own lawful property accumulated through hard work, of the right to land contractual management they enjoy in accordance with law, and of their other lawful rights and interests. Enactment of the property law will serve to define and protect private ownership, condominium right, right to land contractual management and house-site-use right, for the purpose of protecting the immediate interests of the people, stimulating their vigour to create wealth and promoting social harmony.

Enacting the property law is necessitated by the goal of establishing a Chinese-style socialist legal system by 2010. Property law is an important component part of the civil code, playing the role of a prop in the Chinese-style socialist legal system. Enactment of the property law provides an important step taken within the term of the current National People's Congress for giving a basic shape to the Chinese-style socialist legal system.

Wang Zhaoguo's speech was delivered just before the law was to be submitted to the National People's Congress for final deliberation and voting at that session. The speech reveals legislators' desire to draft an official piece of legislation titled the 'property law' as a crucial step in improving the national economic system by making it more responsive to the rapidly changing domestic and international environments.

In this connection, the Property Rights Law is supposed to cover a range of property-related matters, concentrating on property ownership and utilization, with a view to protecting the property rights of all civil subjects on a level playing field and galvanizing people's creativity with a more transparent regime for assuring property rights.

It is in this context that the Property Rights Law was finally passed at that session of the National People's Congress.

A legal framework for the protection of property was in fact already in place prior to the promulgation of the Property Rights Law, though not in the form

Some enterprises attempt to tap into an area outside of the business line specified in their business licences (e.g. a cafeteria may want to engage in the freight forwarding business). It is possible for a contract made under such circumstances to be recognized as having legal force. According to the Supreme People's Court's Interpretation on the Contract Law (I), the court normally will not hold such a contract invalid, unless entering into the contract is in violation of the law that bans the carrying out of such business or contravenes the government policy of restricting or solely controlling the carrying out of such business (Article 10).

Assume that the business licence issued to XYZ (a private enterprise) by the Administration for Industry and Commerce in Beijing documents XYZ's business scope as covering only the food business. Attracted by the lucrative steel business, XYZ recently entered into a number of contracts pertaining to buying and selling steel and profited greatly from these transactions. Although selling and buying steel is not within XYZ's business scope, the contracts thus entered into by XYZ will not be held void by the court unless special permission is statutorily required for engaging in the steel business and XYZ happens to lack such permission.

A void contract

A void contract refers to a contract which seemingly has been created but actually does not have any legal force. Since a void contract is not valid as of its creation. It never has any legal force and thus is not binding on any party to it at any time.

The Contract Law lists five circumstances under any of which a contract made is void: (1) entering into a contract by deceit or duress to undermine national interest; (2) maliciously colluding in undermining the interests of the state, a collective or a third party; (3) concealing an unlawful objective under the disguise of a legitimate form; (4) impairing public interest; and (5) contravening mandatory provisions of laws or administrative regulations (Article 52). Here the term 'mandatory provisions' used in the last circumstance is interpreted under the Supreme People's Court's Interpretation on the Contract Law (II) as those mandatory provisions specifically on 'the validity of a contract' (Article 14).

A void contract does not produce a legally binding effect from the outset; however, if only part of a contract is invalid, then the invalid part will not affect the remaining valid part of the contract (Contract Law, Article 56). Also, the invalidity of a contract does not affect the validity of any term or clause that independently exists in the contract that is specifically pertinent to the settlement of disputes in relation to this contract (Article 57).

In the event of a void contract, any property gained as a result of executing such contract shall be returned; and if the return of the property is not feasible or becomes no longer necessary, corresponding compensation shall be made in cash terms instead (Contract Law, Article 58). Also under the circumstance of a void contract, if a party to the contract has committed a fault causing damage to the other contracting party, he will be liable for his counterparty's loss; but if both parties have been at fault, then each will be held responsible for the outcome caused by each party's own fault (Article 58).

A voidable contract

A voidable contract refers to a contract which is tainted with a defect but has come into force as a valid contract. Its defect may (but will not necessarily) give rise to its revocation subsequently. In other words, due to the existence of a defect, the contract currently in force can be revoked at a certain point in time by a contracting party who is entitled to exercise his right to rescind the contract, provided that he decides to do so. However, if he decides not to revoke the contract, then its validity will not cease even though the defect is not eradicated.

In practice, a voidable contract in the main relates to a contract, the formation of which disobeys a contracting party's true intent. Although such a contract has come into force, since its formation does not represent the contracting party's genuine willingness, it becomes a revocable contract, the validity of which has not been denied presently but which faces the risk of being cancelled at the discretion of a contracting party.

Pursuant to the Contract Law, for a contract made under a material misconception or in an apparently unfair manner, the injured contracting party is entitled to apply to the court or to an arbitral body for revoking the

contract (Article 54, paragraph 1). Also, in the event of a contract made due to deceit or duress or by taking advantage of a contracting party's plight, the injured contracting party who enters into such contract at odds with his true intent is entitled to apply to the court or to an arbitral body for revoking the contract (Article 54, paragraph 2). However, if the injured contracting party merely applies to the court or to an arbitral body for modifying (rather than revoking) the contract, then the court or the arbitral body concerned can only consider the demand for modification and will not be in a position to revoke the contract (Article 54, paragraph 3).

A contract that has been revoked is deemed to have no legally binding effect from the start (Contract Law, Article 56). However, even if a contract is revoked, the revocation does not affect the validity of any term or clause that independently exists in the contract specifically relating to the settlement of disputes in connection with this contract (Contract Law, Article 57).

Under Article 58 of the Contract Law, once a contract is revoked, any property gained as a result of executing the contract shall be returned; and if the return of the property is not feasible or becomes no longer necessary, then the compensation shall be made in cash terms. After a voidable contract in force is revoked, if a contracting party has committed a fault injuring the other contracting party, he will be liable for his counterparty's loss; if both parties have been at fault, then each will be liable for the result arising from each party's own fault (Article 58).

The validity of a contracting party's right to revoke the contract does not last forever. It may end at a certain point in time under specified circumstances. In this regard, the Contract Law lists two circumstances under either of which the validity of a contracting party's right to revoke the contract will cease: (1) if a contracting party who has the right to revoke the contract has not exercised such right for a year, since he knows or ought to have known what has happened that may lead to revocation of the contract; and (2) if a contracting party who has the right to revoke the contract, expressly indicates that he has given up such right, or he has given up such right by his conduct (Article 55).

Here is an example. Bright Star is a shop selling Chinese paintings and calligraphy works. T saw a Li Ming painting, 'Three Horses,' displayed in

Bright Star priced at RMB 50,000. Li Ming (who is deceased) is one of the most noted painters in China, famed for his paintings of horses. The manager of Bright Star assured T that this was a genuine painting by Li Ming. T bought the painting, but later discovered that it was painted by another Li Ming, an unknown young painter with the same name. T never had any interest in buying any of this unknown Li Ming's paintings. T wanted to return the painting to Bright Star for a refund. Bright Star refused to refund T's money, arguing that the painting T bought from Bright Star was not a bogus work so Bright Star did nothing wrong in this transaction. What advice should one give to T? T's true intent is to buy a painting by Li Ming (the deceased famous painter). Thus the deal between Bright Star and T could be deemed to have been accomplished under a material misconception (i.e., they formed a voidable contract). The Contract Law provides that for a contract made under a material misconception or in an apparently unfair manner, the injured contracting party is entitled to apply to the court or to an arbitral body for revoking the contract (Article 54, paragraph 1). Therefore, if the dispute between T and Bright Star could not be resolved by negotiation or consultation in an amicable way, T may consider applying to an arbitral body or to the court for revoking the contract, so that his money would be refunded after returning the painting to Bright Star. Of course, if T decides not to take any action, the deal remains valid.

A contract with undecided validity

A contract with undecided validity refers to a contract that seems to have been made on the face of it but in fact has yet to come into force, subject to whether a third person (other than the contracting party) can ratify or admit its validity or whether the contracting party originally without authority to enter into such contract can subsequently gain the required authority. If the third party does not ratify or admit its validity or the contracting party lacking authority cannot later on acquire the required authority, the contract will still not be able to produce any legal effect.

In the eyes of the Contract Law, a contract with undecided validity mainly relates to a contract entered into by a person with limited capacity for civil conduct, or a contract made without proper authorization of agency, or a contract formed under the circumstance of having no right to transact other people's property.

A contract entered into by a person with limited capacity for civil conduct

Under the General Principles of Civil Law, a minor aged ten or above or a mentally disordered person who is not able to fully account for his own conduct is a person with limited capacity for civil conduct, and normally his civil activities can only be carried out by his agent ad litem on his behalf or by himself with the consent of his agent ad litem (Article 12; Article 13, paragraph 2).

Under the Contract Law, a contract entered into by a person with limited capacity for civil conduct can only become effective after it is ratified by his agent ad litem; however, a contract entered into by such a person under which he purely enjoys rights, or a contract entered into by him that is level with his age, intellectual ability and mental health, can be deemed to be effective from the start with no need to be ratified by his agent ad litem; in the case of his agent ad litem being silent on this matter, it can be taken that the agent ad litem refuses to ratify the contract; before the contract is ratified, his counterparty who has acted in good faith has the right to revoke the contract, and the revocation shall be made by means of having him informed (Article 47).

By the Supreme People's Court's Interpretation on the Contract Law (II), where a person with limited capacity for civil conduct enters into a contract and his agent ad litem ratifies the contract, the ratification will start to take effect when the expression of ratifying the contract made by his agent ad litem reaches him (Article 11).

A contract made without proper authorization of agency

Under the Contract Law, a relevant party may authorize his agent to enter into contracts on his behalf (Article 9, paragraph 2). However, a contract made by a so-called 'agent' without proper authorization of agency cannot acquire any legal force unless it is ratified by the principal.

In this regard, the Contract Law provides that a contract made by a person in the name of a principal under the circumstances that as a matter of fact he has no authorization of agency, or he acts in excess of his authority of agency, or his authority of agency has ended, will not be able to bind the principal if the

principal does not ratify it, but will lead the person in question to face legal consequences; his principal can be urged to ratify the contract within a month, and his principal's silence on this matter will be taken as a refusal to ratify it; his principal's ratification shall be made by means of having him informed (Article 48).

By the Supreme People's Court's Interpretation on the Contract Law (II), where a contract is made in the name of a principal by a person purporting to be that principal's agent who in effect is not, given that the principal has started performing his obligations set out in the contract, such performance will be deemed to be the principal's ratification of the contract (Article 12).

A bona fide third party, which refers to a party to a contract made by a so-called 'agent' without proper authorization of agency, is protected under the Contract Law. If the counterparty in the contract has a good reason to believe that that person in question has authority of agency, then that person's act as the agent will be deemed to be valid and the contract thus formed will be binding (Contract Law, Article 49). In this circumstance, by the Supreme People's Court's Interpretation on the Contract Law (II), the principal can claim compensation against the person who purports to be his agent but in effect has no appropriate authorization of agency for his loss incurred due to the unauthorized act of agency (Article 13).

Another common case is when the deputy of an organization (say, a director or head of a company) enters into contracts on behalf of that organization in excess of the authority given him by the organization. Given that his counterparty in the contract does not know or has no reason to know that he is acting beyond his authority, the contract is valid and binding on the contracting parties (Contract Law, Article 50). That is to say, the contract made will bind the organization.

A contract formed under the circumstance of having no right to transact other people's property

'A contract formed under the circumstance of having no right to transact other people's property' is not uncommon in everyday life.